DRAFT

Marshall Borchert
President Riser Bond Inc
Lincoln Nebr 68501

May 9, 1994

William F. Caton, Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, DC 20554

Re: CC Dkt. No. 94-1

Dear Mr. Caton:

not!

NOT!

We write this letter as CEOs of telecommunications manufacturing companies to urge that the Commission eliminate its regulation which caps the profitability of local exchange telephone companies ("LECs"). As discussed below, we believe eliminating this particular regulation will help stimulate growth in the telecommunications manufacturing industry without creating any serious offsetting risk.

Background

In 1990, the FCC abandoned its longstanding policy of regulating LEC telecommunications services by policing the LECs' "rate of return". Under rate of return regulation, the FCC had set the price of communications services at whatever level was required to ensure that LECs would earn a reasonable profit on the plant and equipment they used to provide these services.

When it abandoned rate of return regulation in 1990, the Commission substituted a new set of rules it called "price cap" regulation.[1/] Price cap rules contain two core features. The first feature forces each LEC to reduce the price at which it offers communications service by at least 3.3 percent each year in after-inflation dollars. The second feature is a carryover from the abandoned rate of return regulation system. Under this feature, a LEC is prohibited from earning a return on investment that exceeds 14.25 percent; any excess profit must be converted to lower prices for communications services the following year. The

---

1/ See Policy and Rules Concerning Rates for Dominant Carriers, 5 FCC Rcd. 6786, 6789-90 (1990), erratum, 5 FCC Rcd. 7664 (1990), recon., 6 FCC Rcd. 2637 (1991), aff'd sub nom. Nat. Rural Telecommun. Ass'n v. FCC, 988 F.2d 174 (D.C. Cir. 1993).

No. of Copies rec'd Copy
List ABCDE

NO

agency explained that this second feature would remain "until we acquire additional experience. . . ."[2]

In the present proceeding, the Commission is reviewing the price cap regulations it adopted in 1990. Among other things, the agency has asked for comments on whether it should eliminate the component of price cap regulation which caps the maximum profit LECs may earn.[3]

Discussion

While the Commission should retain the first component of its price cap rules described above (i.e., requiring an annual reduction in the price of communications services), it should eliminate the second component (i.e., capping LEC profitability) because this feature stifles the growth of the telecommunications manufacturing industry. As the heads of companies which make telecommunications equipment for use in LEC telephone networks, we obviously favor regulatory policies that increase incentives for LECs to deploy cost-saving equipment in their telephone networks. Capping the amount of profit a LEC may earn obviously dampens its incentive to reduce costs and thus dampens its willingness to deploy new cost-cutting technologies.

Not only would eliminating the profit cap facilitate growth in the telecommunications manufacturing industry, the risk of eliminating the cap has grown progressively smaller with each passing year. First, while the Commission's 1990 regulations imposed the earnings cap due to uncertainty about whether the mandatory 3.3 percent price reductions in those rules is large enough to provide LECs with an incentive to cut costs, four years of experience demonstrates that it is. Thus, the Commission itself notes that expenditures by LECs on cost-saving technologies have grown in the last four years.[4] The marketplace also provides a greater incentive now than in 1990 for LECs to cut costs. For example, in the past four years the Commission has eliminated many regulatory barriers that previously were thought to hamper the

---

[2] Id., 5 FCC Rcd. at 6801.

[3] Notice of Prop. Rulemaking in CC Dkt. No. 94-1, FCC No. 94-10 at ¶¶ 52-55 (rel. Feb. 16, 1994). The agency set May 9, 1994, as the deadline for filing comments. Order in CC Dkt. No. 94-1 (DA 94-314, rel. April 7, 1994).

[4] Notice of Proposed Rulemaking, Supra, at ¶ 29.

ability of companies to compete with LECs.[5/] Changes in economic factors also have speeded the growth of competition in the LECs' traditional businesses.[6/]

Conclusion

The Commission should retain the requirement in its price cap rules that LECs reduce prices annually, but it should eliminate the cap on LEC profitability. This action will help stimulate growth in telecommunications manufacturing and will speed the modernization of telephone network infrastructure.

Sincerely,

5/ Id. at ¶ 20.

6/ Id. at ¶¶ 22,24.

Signature Authorization Form

I authorize Rodney L. Joyce to sign my name to a letter to the Federal Communications Commission commenting on the pricing of telecommunications services offered by local exchange telephone companies. I received a copy of this letter as an attachment to a Memorandum to me from Mr. Joyce dated May 3, 1994.

ABSOLUTELY NOT

Signature

Printed Name

Title

Company Name

Please telecopy the signed Signature Authorization Form to Rodney L. Joyce at (202) 637-9195.